

COMMONWEALTH EDISON COMPANY

BEFORE THE

ILLINOIS COMMERCE COMMISSION

DOCKET NO. 01-0423

**PETITION FOR APPROVAL OF DELIVERY SERVICES TARIFFS
AND TARIFF REVISIONS
AND OF RESIDENTIAL DELIVERY SERVICES
IMPLEMENTATION PLAN**

REBUTTAL TESTIMONY

SUBMITTED BY

DAVID J. EFFRON

ON BEHALF OF

**PEOPLE OF THE STATE OF ILLINOIS
CITY OF CHICAGO
COOK COUNTY STATE'S ATTORNEY'S OFFICE
CITIZENS UTILITY BOARD**

OCTOBER 16, 2001

1 **Witness Introduction**

2 Q. Please state your name.

3 A. My name is David J. Effron.

4

5 Q. Have you previously submitted testimony in this docket?

6 A. Yes. I submitted direct testimony marked as Exhibit GC 2.0 and supplemental
7 direct testimony marked as Exhibit GC 2.0 Supplemental. My qualifications,
8 background, and experience are included with my direct testimony, Exhibit GC
9 2.0.

10

11 Q. What is the purpose of this rebuttal testimony?

12 A. The purpose of this rebuttal testimony is to respond to the testimony filed by
13 other parties to this docket. In particular, I respond to the rebuttal testimony of
14 ComEd witnesses Helwig, Juracek, Hill (including supplemental rebuttal), and
15 Voltz (including supplemental rebuttal). I also respond to the direct testimony of
16 IIEC Witness Chalfant on the matter of functionalization of general plant and
17 administrative and general expenses. In addition, I am incorporating certain
18 modifications to my direct testimony based on my supplemental testimony and
19 positions addressed in this rebuttal testimony.

20

1 **Revenue Requirement Effect of Plant Additions**

2 Q. In his rebuttal testimony, Mr. Helwig claims that even if ComEd achieves
3 significant reductions to expenses incurred in 2000, its proposed revenue
4 requirement is still not overstated. Do you concur?

5 A. No. Mr. Helwig presents an analysis that purports to show that even if ComEd
6 can reduce operation and maintenance expenses from the test year level, the
7 revenue requirement effect will be offset by the revenue requirement associated
8 with plant additions taking place after the end of the test year. However, Mr.
9 Helwig's analysis is incomplete and ignores the fact that the establishment of
10 delivery service revenue requirements is not an end in itself, but rather a means to
11 determine rates for delivery service. Mr. Helwig looks solely at revenue
12 requirements rather than looking at the revenues produced by established rates,
13 that is the rates times the billing determinants. An appropriate analysis would
14 take into account the revenues produced by rates derived from a given revenue
15 requirement, rather than just examining changes in the revenue requirement itself.

16
17 Q. Have you prepared an analysis that demonstrates the effect of plant additions on
18 revenue requirements and the extent to which this effect could offset reductions to
19 O&M expenses in the determination of rates?

20 A. Yes. My Schedule DJE-10 accompanying this rebuttal testimony shows the effect
21 of plant additions on revenue requirements and the resulting rate implications. I
22 have excluded general plant and A&G expense from this analysis because: 1)
23 capital costs of distribution plant and distribution O&M are the main components

1 of revenue requirements; 2) the abnormal expenses in 2000, with relatively minor
2 exceptions, were not charged to A&G; and 3) there is a dispute as to how the
3 general plant and A&G should be functionalized to delivery services.

4 The first column on this schedule shows the elements of revenue
5 requirements related to distribution plant and distribution O&M (including
6 customer operations expenses). I have used the adjusted test year balances as
7 presented by ComEd as my starting point in this column, and I have used the rate
8 of return proposed by City of Chicago Witness Walter, grossed up for income
9 taxes, to calculate the return requirement on net plant. The revenue requirement
10 for distribution plant and distribution O&M is \$1.452 billion. If sales for the year
11 are 85,000,000 mWh, the necessary average rate for these cost elements is
12 \$0.017080 per kWh.

13 I have assumed annual distribution plant additions of \$400 million in this
14 analysis. This approximates the distribution plant additions in 2000, exclusive of
15 any transfers from other functions. It should be noted that the distribution plant
16 additions in 2000 were the highest of any of the years 1995-2000, again exclusive
17 of any transfers from other functions. As these plant additions take place, the
18 accumulated reserve for depreciation will also be growing. To calculate the
19 growth in the depreciation reserve, I added the annual depreciation on distribution
20 plant for the test year plus one-half of the annual depreciation expense on the
21 plant additions, a total of \$274.6 million. Thus, the increase in distribution plant
22 net of accumulated depreciation is \$125.4 million. The return requirement on this
23 increase in net plant is \$15.7 million.

1 There is also a revenue requirement associated with the depreciation
2 expense on the plant additions. Using the composite depreciation rate for plant
3 additions from ComEd Exhibit 4.0, Appendix C, Schedule C-2.1, the depreciation
4 expense on the plant additions is \$10.2 million. Thus, the total incremental
5 revenue requirement associated with the \$400 million of plant additions is \$25.9
6 million. I should point out that this calculation is quite conservative because it
7 does not account for any increases in accumulated deferred taxes and operating
8 reserves, both rate base deductions, that will likely be taking place as the plant
9 balance grows. In addition, I have not taken into account the fact that ComEd has
10 already adjusted rate base for certain post-test year plant additions and that actual
11 distribution plant additions after the test year will thus not be entirely incremental
12 to plant already included in rate base. Further, I have excluded the effect of any
13 plant retirements, which would be neutral as to the return requirement but would
14 reduce depreciation expense.

15
16 Q. Aside from your reservations regarding those factors, does your analysis then
17 show that ComEd could reduce operation and maintenance expense by \$25.9
18 million and still not have a revenue excess?

19 A. No, such a conclusion would be wrong. Like Mr. Helwig's testimony, this
20 analysis so far ignores any additional revenue that will be produced by growth in
21 billing determinants taking place after the end of the test year. As I show on
22 Schedule DJE-10, with a growth rate in billing determinants of only 1%,
23 additional revenue of \$14.5 million would be produced by rates based on a

1 revenue requirement of \$1.452 billion. This implies that an expense reduction of
2 \$11.4 million would totally offset the incremental revenue requirement associated
3 with the distribution plant additions. With a growth rate in billing determinants
4 of 2%, the Company could incur \$3.2 million **more** in O&M expenses and still
5 not have a revenue deficiency.

6

7 Q. Is a growth rate of 2% realistic?

8 A. Yes. The revenue requirement presented by ComEd in this case represents an
9 increase of 47.5% over the revenue requirement approved by the Commission in
10 Docket No. 99-0117. Yet ComEd Exhibit 1.0, page 20, shows a requested
11 average rate increase of “only” 36.7%. This implies growth in billing
12 determinants of 7.9% since the test year in Docket No. 99-0117, which was three
13 years before the test year in this case. Annual growth of approximately 2.6% per
14 year produces an increase of 7.9% over three years. Based on this experience, a
15 2% growth rate is not only reasonable, but may be conservative. With a growth
16 rate in billing determinants of 2.6%, the Company could incur \$11.9 million
17 **more** in O&M expenses and still not have a revenue deficiency because of
18 additions to distribution plant.

19

20 Q. What do you conclude?

21 A. The Commission should disregard Mr. Helwig’s testimony on the expense
22 reduction that ComEd could achieve without a decrease to its revenue
23 requirement. It is inaccurate and incomplete. It is of no value to the Commission

1 in its consideration of the extent to which expenses incurred by ComEd in 2000
2 should be adjusted. If expenses incurred in 2000 were excessive or abnormal, or
3 if expenses will decrease prospectively because of merger savings, then O&M
4 expenses should be adjusted accordingly in determining rates for delivery service,
5 Mr. Helwig's testimony to the contrary notwithstanding.

6

7 **Normality of Test Year**

8 Q. On page 15 of her rebuttal testimony, Ms. Juracek states that ComEd's revenue
9 requirement should not be reduced because of claims that its annual expenses or
10 additions to rate base were excessive. Do you have a response?

11 A. Yes. I agree that ComEd's revenue requirement should not be reduced because of
12 claims that its annual expenses were excessive. ComEd's revenue requirement
13 should be reduced if its expenses were, in fact, excessive. That is, if the expenses
14 incurred in 2000 were excessive or abnormal, then the Commission should adjust
15 those expenses to a normal level in determining ComEd's revenue requirement.
16 The prospective delivery service rates should be established to recover a normal
17 level of expenses, not an excessive or abnormal level of expenses.

18

1 **Audit of Plant Additions**

2 Q. On page 38 of her rebuttal testimony, Ms. Juracek describes the request for an
3 audit of ComEd's plant additions to be "merely a delaying tactic" to postpone the
4 date on which new rates from this case would take effect. Did you propose an
5 audit of ComEd's plant additions in order to delay the date on which new rates
6 from this case would take effect?

7 A. Not at all. Nowhere did I say, or even imply, in my direct testimony that new
8 rates should not be implemented on May 1, 2002. However, implementation of
9 new rates at that time does not preclude an audit of ComEd's plant additions and
10 does not eliminate the necessity of such an audit.

11

12 Q. Assuming that ComEd's decisions to make the plant additions in question were
13 prudent, is an audit therefore unnecessary?

14 A. No. Ms. Juracek states that when necessary investments are identified, there is
15 nothing imprudent about making those investments. However, this provides no
16 insight into whether the costs of those investments, and the associated revenue
17 requirements, are reasonable. As I explained in my direct testimony, unreasonable
18 costs may arise from a number of sources, such as premiums for expedited
19 construction schedules and escalation of costs due to delays. In the circumstances
20 of this case, where the plant in rate base may well include such excess costs, an
21 audit of the costs of the plant additions is necessary to determine if any of the
22 costs of ComEd's distribution infrastructure improvements were avoidable and,
23 therefore, unreasonable.

1

2 **Functionalization**

3 Q. Mr. Effron, have you reviewed Mr. Hill's rebuttal testimony on the
4 functionalization of general plant and administrative and general expenses?

5 A. Yes. Mr. Hill addresses this matter at pages 4-9 of his rebuttal testimony.

6

7 Q. Does anything in his rebuttal testimony cause you to reconsider your position on
8 the functionalization of general plant and administrative and general expenses?

9 A. No. Mr. Hill has presented no persuasive reason why the Commission should
10 change the method of functionalizing general plant and administrative and
11 general expenses that it approved in Docket No. 99-0117.

12 With regard to the functionalization of general plant, the Commission
13 stated in that docket that it:

14 ... disagrees with Edison's direct assignment approach. The very
15 nature of these costs suggests that they are not amenable to direct
16 assignment. In previous cases, Edison used a labor allocator to
17 assign these costs. Edison has not made a convincing argument for
18 deviating from this past practice. Accordingly, IIEC's proposed
19 labor allocator for general plant is reasonable and should be
20 approved.

21

22 (Order, page 11)

23

24 Similarly, with regard to the functionalization of administrative and
25 general expenses, the Commission stated that:

26 While direct assignment may be a better method in some cases, the
27 Commission does not believe costs, which include CEO and
28 executive salaries, are amenable to direct assignment. Were such
29 costs amenable to direct assignment, Edison would have assigned
30 these costs directly to the distribution function in prior cases.
31 Edison did not. For the same reasons that we disagreed with

1 Edison's direct assignment of General Plant costs, we also disagree
2 with Edison's direct assignment of A&G expenses. We, therefore,
3 adopt IIEC's proposal for allocation.
4

5 (Order, page 27)
6

7 The general plant and administrative and general expenses to be
8 functionalized are of substantially the same nature in this case as they were in
9 Docket No. 99-0117. Mr. Hill does not contend otherwise. While Mr. Hill
10 generally describes changes in the Company's organization and accounting that
11 he asserts would limit the categories of costs requiring functionalization through
12 the use of an allocator, as far as I can tell, he has not presented any specific
13 examples of expenses that were not amenable to direct assignment in Docket No.
14 99-0117 that are now amenable to direct assignment as a result of the Company's
15 re-alignment. In my opinion, Mr. Hill has not presented an adequate justification
16 for modifying the functionalization method approved by the Commission in
17 Docket No. 99-0117.
18

19 Q. Have you read IIEC Witness Chalfant's testimony on the functionalization of
20 general plant and administrative and general expenses?

21 A. Yes. Mr. Chalfant also recommends that a labor allocator be used to
22 functionalize general plant and administrative and general expenses. However,
23 his proposal appears to differ from mine in that he does not use the labor allocator
24 to functionalize intangible plant, whereas I do.
25

26 Q. Why do you use the labor allocator to functionalize intangible plant?

27 A. The Company includes intangible plant together with general plant in the
28 determination of its rate base. Therefore, it seems reasonable to use the same
29 allocator to functionalize general plant and intangible plant.
30

31 Q. Did the Commission approve the use the labor allocator to functionalize
32 intangible plant in Docket No. 99-0117?

33 A. The Commission did not explicitly address the functionalization of intangible
34 plant in its order in Docket No. 99-0117, so I cannot tell from the Order the
35 method that was approved to functionalize intangible plant in that case. However,
36 the gross balance of intangible plant in 1997, the test year in Docket No. 99-0117,
37 was only \$80,000. Given the immaterial balance of intangible plant, the method
38 used to functionalize it in Docket No. 99-0117 would have had no effect on the
39 determination of rates for delivery service. Further, in Docket No. 99-0120/0134,
40 concerning the Illinois Power Company, general plant and intangible plant were
41 treated together and the Commission approved the use of a labor allocator to
42 functionalize all this plant. In Illinois Power's current delivery services tariff
43 case, Docket No. 01-0432, that company uses a labor allocator to functionalize
44 both general and intangible plant. Mr. Chalfant has presented no reason why
45 ComEd's intangible plant should be functionalized differently from general plant.
46

1 **Uncollectible Accounts**

2 Q. Have you reviewed Mr. Hill's testimony regarding uncollectible accounts
3 expenses?

4 A. Yes, and I must admit that I find it somewhat confusing. Mr. Hill states that he
5 disagrees with my proposed adjustment to uncollectible accounts expense. Yet,
6 he goes on to say that he does agree that if the revenue requirement is adjusted,
7 then a corresponding adjustment to uncollectible accounts expense "would be
8 necessary." Thus, to the extent that my adjustment to uncollectible accounts
9 expense is related to a change in the revenue requirement, which it is in part, Mr.
10 Hill appears to agree that it is appropriate.

11 Mr. Hill also states that the Company's uncollectible accounts expense is
12 based on an analysis of uncollectible account expense activity by customer class
13 for the year 2000. This sounds like the very method of determining uncollectible
14 accounts expense rejected by the Commission in Docket No. 99-0117. On the
15 other hand, I believe my method is substantially the same as that approved by the
16 Commission in Docket No. 99-0117.

17 I can find no explanation in Mr. Hill's testimony of why the Commission
18 should abandon the method of determining uncollectible accounts expense that it
19 approved in Docket No. 99-0117 for a method that it rejected in that docket. As
20 Mr. Hill does not take the position that my method of calculating uncollectible
21 accounts expense is inconsistent with the method approved by the Commission in
22 Docket No. 99-0117, the basis for his disagreement with my proposed adjustment
23 is unclear to me.

24
25 **Taxes Other Than Income Taxes**

26 Q. Does Mr. Hill address your proposed adjustment to state use tax on purchases in
27 his rebuttal testimony?

28 A. Yes. Again, however, I am uncertain whether he disagrees with my proposed
29 adjustment. I did not propose the entire elimination of this expense in my
30 testimony. Therefore, my position is not inconsistent with any of the points
31 raised by Mr. Hill at ComEd Exhibit 23.0, page 23, lines 494-499. In addition,
32 Mr. Hill, with apparent approval, cites my treatment of state use tax on purchases
33 at ComEd Exhibit 23.0, page 23, lines 504-506. Yet, he does not recommend that
34 the Commission adopt my adjustment. If Mr. Hill is sticking to his original
35 position that three years' worth of state use tax on purchases should be included
36 in test year revenue requirements, then I disagree with his rebuttal testimony on
37 this matter. If he is endorsing the treatment of state use tax on purchases
38 presented in my direct testimony, then I obviously have no disagreement with Mr.
39 Hill on this issue.

40
41 Q. Does Mr. Hill also address your proposed adjustment to real estate taxes in his
42 rebuttal testimony?

43 A. Yes. First, Mr. Hill explains how the Company functionalized real estate taxes,
44 which has nothing to do with my proposed adjustment. Next, Mr. Hill addresses

1 my five-year averaging methodology, which he criticizes for failing to exclude an
2 outlier. On further consideration and review of the data, I have modified my
3 proposed adjustment to eliminate the outlier from the five-year average that I
4 used. I have incorporated the modified adjustment into calculation of the revenue
5 requirement accompanying this testimony. On my Schedule DJE-4R, my
6 adjustment to real estate taxes is the same as quantified by Mr. Hill in his rebuttal
7 testimony, ComEd Exhibit 23.0, at page 24, lines 524-527.
8

9 Q. Mr. Hill also addresses adjustments to the Illinois Electricity Distribution Tax
10 expense to eliminate an inadvertent error in his rebuttal testimony. Have you
11 incorporated these adjustments into your calculation of revenue requirements?

12 A. Not at this time. In City of Chicago Data Request 52, the Company was asked to
13 provide calculations supporting the Illinois Electricity Distribution Tax expense
14 for the test year. Rather than responding with the requested information, the
15 Company described the method of determining the Illinois Electricity Distribution
16 Tax and cited what it believed were certain corrections that should be made to the
17 tax expense booked in 2000. The best way to determine the test year Illinois
18 Electricity Distribution Tax expense for the test year would be calculate the actual
19 liability based on the appropriate tax rates and tax base. To my knowledge, the
20 Company has not provided the data that would permit such a calculation.
21 Therefore, I have not incorporated the adjustments to the Illinois Electricity
22 Distribution Tax described in Mr. Hill's rebuttal testimony.
23

24 **Merger Savings**

25 Q. In his rebuttal testimony, Mr. Hill states that he opposes your adjustment to
26 recognize merger savings. Do you have a response?

27 A. Yes. Mr. Hill first states that my adjustment relates to estimates of savings that
28 are neither known nor measurable. I disagree. It is known that the merger will
29 produce savings. As I stated in my direct testimony, the Exelon Corporation SEC
30 Form 8-K dated March 16, 2001 states that approximately 2,900 positions have
31 been identified to be eliminated as a result of the Merger Transaction. The
32 elimination of these positions will certainly result in reductions to expenses. As
33 far as I know, none of the Company witnesses contend that there will be no
34 savings from the elimination of these positions or assert that such savings will not
35 affect expenses incurred by ComEd in the provision of delivery services.

1 I also believe that such savings are measurable with reasonable certainty.
2 However, because ComEd declined to provide information that would have
3 permitted a more precise measurement of such merger savings, I had to rely on
4 the estimating method described in my direct testimony to quantify the necessary
5 adjustment to reflect merger savings.

6 Mr. Hill then goes on to say that my proposed adjustment reflects impacts
7 that will not be realized until far beyond the end of the test year in this
8 proceeding. Earlier in his rebuttal testimony, however, Mr. Hill stated that
9 employee departures would begin taking place in September 2001, which is
10 approximately nine months after the end of the test year. I do not consider this to
11 be an unreasonably long time after the end of the test year for the purpose of
12 recognizing an adjustment of this nature, as this adjustment reflects a material
13 change from the relationships that existed during the test year. This change will
14 affect the revenue requirements, both absolute and relative to billing
15 determinants, when the rates established in this case are in effect.

16 The last criticism of my merger savings adjustment offered by Mr. Hill is
17 that I used an "extraordinarily long" period to amortize the costs of achieving
18 merger savings. I used a period of ten years to amortize the costs to achieve.
19 While the appropriate amortization period is clearly a matter of judgment, and I
20 cannot state absolutely that any different amortization period would be incorrect,
21 I believe that a ten-year amortization is reasonable for the costs to achieve savings
22 in that: 1) the savings from the merger will continue indefinitely; and 2) much of
23 the costs to achieve the savings are in the form of enhanced retirement benefits

1 that will be paid out over many years. The fact that I used a five-year average for
2 quantifying normalization adjustments is completely irrelevant to this issue, as the
3 periods used to calculate normal expenses have nothing to do with the appropriate
4 period over which any costs, including costs to achieve merger savings, should be
5 amortized. Similarly, the amortization period for rate case expense is irrelevant,
6 as this is meant to represent the expected period between rate cases. If the
7 expected period between mergers were used to amortize the costs to achieve and
8 if history is any guide, the amortization period could well be longer than ten
9 years, not shorter.

10

11 Q. Mr. Effron, since the preparation of your direct testimony, have you reviewed
12 additional information regarding the savings that ComEd can expect to realize as
13 a result of the merger?

14 A. Yes. I have reviewed the redacted response to Staff Data Request BCS-1.23
15 (Confidential). This response contains a forecast of the payroll savings to ComEd
16 as result of positions that will be eliminated because of the merger. Based on my
17 review and analysis of this response, I continue to believe that the estimate of
18 merger savings for ComEd delivery services contained in my direct testimony is
19 reasonable.

20

21 **Incentive Compensation**

1 Q. With regard to your adjustment to incentive compensation, Mr. Hill states that
2 your adjustment is based on the “unsupported premise” that a five-year average is
3 representative of a normal level of expense. Do you have a response?

4 A. Yes. Mr. Hill has offered no evidence that the actual incentive compensation
5 expense incurred in 2000 is more representative of the likely ongoing normal
6 level of incentive compensation than is my proposed five-year average. I
7 explained why I believe a five-year average should be used in my direct
8 testimony. Mr. Hill has not responded to the specifics of that testimony. ComEd
9 Exhibit 22.0, which Mr. Hill cites in support of his position that a five-year
10 average should not be used, says nothing about the use of actual 2000 incentive
11 compensation rather than a five-year average. In fact, ComEd Exhibit 22.0 does
12 not address the reasonableness any particular level of incentive compensation,
13 only whether the practice of including incentives in employees’ total
14 compensation is reasonable in theory.

15

16 **Accumulated Reserve for Depreciation**

17 Q. Mr. Hill describes your proposed adjustment to the accumulated depreciation
18 reserve on distribution plant as “a proposed change to the test year.” Is this
19 description accurate?

20 A. Absolutely not. My proposed adjustment to the depreciation reserve is no more a
21 proposed change to the test year than is the Company’s proposed adjustment to
22 rate base for additions to distribution plant taking place in 2001. If Mr. Hill is
23 concerned about the purity of the test year, then he should retract his proposed

1 adjustment to rate base for post-test year additions to distribution plant. Then my
2 adjustment to the accumulated depreciation reserve on distribution plant would
3 not be necessary.

4 Mr. Hill's statement that I am proposing a June 30, 2001 test year for
5 accumulated reserve for depreciation of distribution plant is simply false. I am
6 proposing to recognize growth in the depreciation reserve on distribution plant
7 that is consistent with the adjustment for post-test growth in plant that the
8 Company is proposing. Reference to my proposed adjustment shows that I am
9 not recommending that the total accumulated reserve for depreciation of
10 distribution plant as of June 30, 2001 be deducted from plant in service.

11

12 **Normality of O&M Expenses**

13 Q. In their rebuttal testimony, do Company witnesses address your proposed
14 adjustments to the abnormal level of expenses incurred in 2000?

15 A. Yes. Company Witnesses Hill and Voltz address the normality of expenses
16 incurred in 2000 in their rebuttal testimony and supplemental rebuttal testimony.

17

18 Q. In general, how would you describe their position on the normality of expenses
19 incurred in 2000?

20 A. Their position seems to be that, with the exception of certain adjustments in the
21 Company's direct testimony, the expenses in 2000 were normal simply because
22 ComEd actually incurred the expenses in that year. The Company, however, has

1 presented no evidence that the levels of expense incurred in 2000 will continue
2 during the period that the rates established in this case will be in effect.

3

4 Q. Just because the Company incurred the expenses in 2000, does this mean that they
5 are normal?

6 A. No. I agree that as a general proposition it would be unreasonable to require
7 proof of the normality of all test year expenses in the absence of any evidence that
8 actual expenses incurred in the test year were abnormal. However, I believe that
9 in the present case there is strong evidence that expenses incurred in the test year
10 were abnormal, and the Company has done little or nothing to refute that
11 evidence.

12

13 Q. Did you cite any such evidence that the operation and maintenance expenses
14 incurred in 2000 were abnormal in your direct testimony?

15 A. Yes. In my direct testimony, I cited the increase in operation and maintenance
16 expenses since the test year in Docket No. 99-0117, which was 1997. I noted the
17 failure of the Company to explain the reasons for the magnitude of the increases
18 in expenses from the level of expenses found to be reasonable by the Commission
19 only a short time ago. In addition, I have presented comparisons of expenses
20 incurred in 2000 to the level of expenses incurred in other recent years.

21

22 Q. Has ComEd provided any explanation of the reasons for the increases in operation
23 and maintenance expenses since the test year in Docket No. 99-0117?

1 A. Other than some vague generalizations, ComEd has provided absolutely no
2 explanation of the increases in operation and maintenance expenses since the test
3 year in Docket No. 99-0117. Rather, ComEd, has concentrated its explanations
4 on increases in expenses from 1998 and 1999 to 2000. Even then, the Company's
5 explanations have been limited to citing the areas of increased spending, with no
6 attempt to establish that such increases are normal and continuing in nature.
7 Further, referring to Schedules DJE-1S and DJE-2S accompanying my
8 supplemental direct testimony, it can be seen that in the accounts with the largest
9 increases, 580, 590, 592, and 903, there were substantial jumps in expense levels
10 from 1997 to 1998, which the Company has not addressed.

11
12 Q. One factor cited by ComEd for in the increase in distribution operation and
13 maintenance expense is refunctionalization. Is this explanation valid?

14 A. Based on my analysis, it is not. First, on Schedule DJE-1A.R accompanying this
15 testimony, I have recast my analysis of the revenue requirement increase since
16 Docket No. 99-0117. In this new analysis, I have compared distribution operation
17 and maintenance expense in this case to distribution plus transmission operation
18 and maintenance expenses in Docket No. 99-0117. (I have also now included
19 customer accounts expenses and customer information and services expense
20 together as customer operations expense.) This comparison recognizes the effect
21 of transmission expense refunctionalized to distribution in Docket No. 99-0117.
22 The increase in distribution operation and maintenance expenses since Docket
23 No. 99-0117 in this analysis is \$188.4 million, or 82%. As I have already

1 included refunctionalized transmission expenses in Docket No. 99-0117 with
2 distribution expenses, none of this \$188.4 million increase can be explained by
3 refunctionalization from transmission to distribution.

4 Second, if the increase in distribution expenses can really be explained by
5 refunctionalization from transmission, then one would logically expect that such
6 increase in distribution expense would be offset by a commensurate reduction to
7 transmission expense. The transmission operation and maintenance expenses
8 from 1995 through 2000 were as follow:

9	1995	45,549,000
10	1996	45,440,000
11	1997	49,275,000
12	1998	39,393,000
13	1999	69,043,000
14	2000	62,277,000

15
16 While there was a decline in transmission expense from 1999 to 2000, this
17 is only true because the expense in 1999 is significantly greater than the expense
18 in any of the other years. Even with the decrease from 1999, the transmission
19 expense incurred in 2000 still represents an increase of 58% over the expense in
20 1998 and an increase of 26% over the expense in 1997. In addition, the decrease
21 in transmission expense from 1999 to 2000, \$6.8 million, is nowhere near as great
22 as the \$27 million increase in distribution expense that the Company attributes to
23 refunctionalization. Refunctionalization does not explain the magnitude of the
24 increase in distribution operation and maintenance expense in recent years.
25

1 Q. Turning now to the Company's rebuttal testimony with regard to the normality of
2 expenses in specific accounts, have you reviewed Mr. Hill's rebuttal testimony
3 regarding expenses charged to Account 580?

4 A. Yes. As I explained in my direct testimony, the main reason for the increase in
5 Account 580 from 1999 to 2000 was the change in the level of incentive
6 compensation charged to that account. In his rebuttal testimony, Mr. Hill states
7 that incentive compensation related to distribution operations was charged to
8 Accounts 920/921 in 1999 but to Account 580 in 2000. Mr. Hill thus concludes
9 that the increase in Account 580 related to incentive compensation is due to a
10 change in the accounting for incentive compensation rather than an increase in
11 incentive compensation for distribution operations. Mr. Voltz endorses this
12 conclusion in his rebuttal testimony. However, the total incentive compensation
13 for transmission and distribution in 1999 was \$12.2 million, whereas the incentive
14 compensation for distribution alone was \$39.5 million in 2000, an increase of at
15 least \$27.3 million. While part of the increase in Account 580 may result from a
16 change in accounting, clearly the main reason for the increase in expense is a real
17 increase in the level of incentive compensation for distribution operations.

18

19 Q. In his supplemental rebuttal testimony, Mr. Hill claims that you changed your
20 approach to various costs so as to choose lines of attack that result in larger
21 downward adjustments, with no analysis of the revenue requirement as a whole.
22 Is this an accurate characterization of your testimony?

1 A. It is not. On pages 4-8 of my direct testimony, I explicitly addressed the
2 normality of expenses incurred in 2000 in the context of the Company's overall
3 revenue requirement. I also compared the delivery service revenue requirement
4 claimed by the Company in this case to that approved by the Commission in
5 Docket No. 99-0117 and analyzed the reasons for the claimed increase. Contrary
6 to Mr. Hill's assertion, my analysis of the revenue requirement as a whole is the
7 background against which I propose my normalization adjustments.

8

9 Q. Mr. Hill also addresses your proposed adjustment to Account 903, Customer
10 Records and Collection Expenses, in his supplemental rebuttal testimony. Do you
11 have a response?

12 A. Yes. On page 10 of his supplemental rebuttal testimony, Mr. Hill criticizes me
13 for excluding 1999 from the years that I use as a base to quantify my proposed
14 normalization adjustment to Account 903. First, he states that I have simply
15 opined that 1999 appears as an outlier, without offering any further basis. This
16 assertion is untrue. I also cited the response to City of Chicago Data Request
17 1.098 as a basis for my conclusion that the \$170 million of expenses charged to
18 Account 903 in 1999 contains expenses that are abnormal and of a non-recurring
19 nature. Second, Mr. Hill states that he sees no legitimate reason to remove certain
20 years' data when averaging costs. Mr. Hill's criticism is completely inconsistent
21 with his own testimony that data for the year 1996 must be excluded as an outlier
22 in the calculation of the average true-up accrual for real estate taxes, without even
23 an explanation of the factors causing that year to be an outlier (ComEd Exhibit

1 23.0, page 24). The exclusion of 1999 from the base years used to calculate the
2 normalization adjustment to Account 903 is as valid as the exclusion of data for
3 the year 1996 in the calculation of the average true-up accrual for real estate
4 taxes.

5 Mr. Hill also criticizes me for not reflecting the change in accounting for
6 expenses that had been charged to Account 912 in the calculation of my
7 adjustment to Account 903. I agree with this observation. Therefore, I have
8 modified my adjustment to reflect this change in accounting. In Docket No. 99-
9 0117, the Commission found that \$6.3 million of expenses charged to Accounts
10 911 and 912 in 1997 should be reclassified to Accounts 903 and 908. I have
11 conservatively assumed that the full amount of this \$6.3 million would be
12 reclassified to Account 903 and have modified my proposed adjustment
13 accordingly (Schedule DJE-2.3R1).

14

15 Q. In his supplemental rebuttal testimony, Mr. Voltz provides limited explanations
16 for the increases in Accounts 580, 590, 592, 593, and 594 from 1998 to 2000. Do
17 his explanations establish the normality of the expenses charged to these accounts
18 in 2000?

19 A. No. I have already addressed the fallacy of attributing the increase in Account
20 580 to a change in accounting for incentive compensation and problems in
21 attributing increases in distribution O&M to refunctionalization. Mr. Voltz also
22 cites other “drivers” causing the increases to those accounts. However, he has not

1 provided any evidence that the “drivers” causing the increases will continue to
2 have any effect prospectively.

3 For example, with regard to Account 592, Mr. Voltz cites “increased
4 substation maintenance of \$15.1 million” as a “principal driver” of the increase in
5 Account 592 from 1998 to 2000. This is hardly surprising, as Account 592 is
6 “Maintenance of Station Equipment.” This circular explanation offered by Mr.
7 Voltz provides absolutely no insight as to whether the increased level of expense
8 for substation maintenance in 2000 will be incurred on a continuing basis
9 prospectively. Similarly, while Mr. Voltz offers brief descriptions of other
10 “principal drivers” for expense increases in 2000, there is no indication whether
11 the increased level of expenses in 2000 is permanent.

12 Mr. Voltz also takes exception to my inclusion of the years 1995 and 1996
13 in the base for normalization, stating that the expenses incurred in those years
14 have already been accounted for in the previous delivery services rate case
15 because they were incurred before the test year in that case. It is true that 1997
16 was the test year in the last case, but I do not see how that implies that expenses
17 incurred in 1995 and 1996 were somehow “accounted for” in that case. The fact
18 that 1995 and 1996 were prior to the test year in that case is irrelevant to the issue
19 of whether it is appropriate to include those years in the base for a normalization
20 adjustment. I included those years because a five-year period is generally a
21 reasonable basis for establishing a normal level of expenses.

22

1 Q. Mr. Effron, are the total operation and maintenance expenses that you are
2 proposing to include in the delivery services revenue requirement, after your
3 normalization adjustments, reasonable?

4 A. Yes. On my Schedule DJE-1B, I present a comparison of my proposed total
5 operation and maintenance expenses, after my normalization adjustments, to the
6 total operation and maintenance expenses included in the delivery services
7 revenue requirement by the Commission in Docket No. 99-0117. For the purpose
8 of this comparison, I have included transmission expense in the delivery services
9 revenue requirement in Docket No. 99-0117 with distribution O&M expense in
10 that docket. I have also excluded the effect of my proposed adjustment to
11 recognize merger savings in this case.

12
13 Q. Why have you excluded the effect of your proposed adjustment to recognize
14 merger savings?

15 A. The adjustment to recognize merger savings reflects a change that was not in
16 effect in the test year in the last case or the test year in this case. It represents
17 savings that the Company will achieve irrespective of any normalization of test
18 year expenses. It is not relevant to an analysis of the reasonableness of my
19 proposed normalization adjustments.

20
21 Q. What do you conclude from the comparison on Schedule DJE-1B?

22 A. As shown on this schedule, the total O&M, as adjusted, in my delivery services
23 revenue requirement represents an increase of 13.3% over the total operation and

1 maintenance expense included in the delivery services revenue requirement by the
2 Commission in Docket No. 99-0117. Thus, my normalized O&M expenses
3 represent an increase of 13.3% over the O&M expenses found by the Commission
4 to be just and reasonable in a case with a test year just three years before the test
5 year in this case. In this regard, my normalized O&M expenses cannot be
6 criticized as being unreasonably low.
7

8 **Revenue Requirement**

9 Q. Have you prepared updated schedules that incorporate the modifications that you
10 presented in your supplemental testimony and the modifications that you have
11 addressed in this rebuttal testimony?

12 A. Yes. I have prepared Exhibit GC 5.1. This exhibit incorporates my supplemental
13 testimony and the positions addressed in this rebuttal testimony. I have also
14 incorporated the rate of return testimony of City of Chicago Witness Walter.
15 With these modifications, I have calculated a net delivery services revenue
16 requirement of \$1,380,655,000.
17

18 Q. Does this conclude your rebuttal testimony?

19 A. Yes.
20
21